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IN THE

Supreme Court of the United States

OCTOBER TERM, A. D. 1940.

Nos. 281 and 282

WEIGHTSTILL WOODS, COURT TRUSTEE,

281 *Petitioner,*

vs.

CITY NATIONAL BANK AND TRUST COMPANY OF CHICAGO, ET AL.

WEIGHTSTILL WOODS, COURT TRUSTEE,

282 *Petitioner,*

vs.

CITY NATIONAL BANK AND TRUST COMPANY OF CHICAGO, ET AL.

ON WRITS OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SEVENTH CIRCUIT.

PETITION FOR REHEARING.

VINCENT O'BRIEN,
JOHN MERRILL BAKER,
TRACY WILSON BUCKINGHAM,
Attorneys for Petitioners-Respondents.

THE GUNTHORP-WARREN PRINTING COMPANY, 810 WEST JACKSON, CHICAGO

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PETITION FOR REHEARING.

Now come the respondents, City National Bank and Trust Company of Chicago, as Successor Trustee, *et al.*, by their attorneys, and present this their petition and ask that a rehearing be granted to them in the above entitled cause, and that upon such rehearing the judgment of the Circuit Court of Appeals be affirmed. Respondents present herewith their suggestions in support of this petition.

VINCENT O'BRIEN,
JOHN MERRILL BAKER,
TRACY WILSON BUCKINGHAM,
Attorneys for Respondents.

SUGGESTIONS.

As we understand the court's decision, all compensation is denied respondents because of their representation of alleged dual or conflicting interests.

As to the City National Bank and Trust Company, the grounds are:

1. That it formed and dominated the Committee, two members of which were officers of the bank and two of which were officers or employees of one of the underwriters, and at the same time acted as Successor Trustee under the mortgage indenture.

2. That that underwriter not only owned common stock of the debtor company but was later claimed to have been liable for alleged circular misrepresentations.

3. That it was also Indenture Trustee for adjoining properties and dominated the Committees representing them, although the property of the debtor company was selling service to the other two.

As to counsel, the grounds are:

(a) That they represented both the Indenture Trustee and the Committee in the case of the Granada.

(b) That they represented the Indenture Trustee and the Committees for the adjacent properties.

(c) That they had acted as general counsel for Chicago Trust Company, one of the underwriters whose prospectus was under attack in these proceedings.

Because of the prior representation of these conflicting interests, both the Bank and counsel are denied compensation, not only for services rendered while the conflict existed, but also for the services rendered in the 77B proceedings, where there was no conflicting representation.

As to the Point That the Bank Formed and Dominated the Committee, Two Members of Which Were Officers of the Bank and Two of Which Were Officers or Employees of One of the Underwriters, and at the Same Time Acted as Successor Trustee Under the Mortgage Indenture—

There was no contention in the trial court that respondents should be denied compensation on this ground. No mention of it is made in the court trustee's objections (R. 127), nor in the District Court's opinion (R. 761), nor in the detailed and voluminous findings prepared by the court trustee and entered months after the opinion (R. 769). Finding 42 (R. 784) is the only one at all pertinent. The sense of that finding is that it was improper for the Committee, the Bank and counsel to continue to represent more than one of the three adjacent properties. There is no intimation that as to any one of those properties it would have been improper for the Bank to act as Indenture Trustee and at the same time to form and dominate the Committee. Indeed, the inference of the finding is that it was quite permissible for it to do so.

To the extent, therefore, that the decision of this court rests on this point, the respondent is deprived of its day in court. *Lutcher and Moore Lumber Co.* v. *Knight,* 217 U. S. 257, 267; *Magruder* v. *Drury,* 235 U. S. 106; *J. M. Robinson & Co.* v. *Belt,* 187 U. S. 41, 23 S. Ct. 16.

We submit that the court overlooked this point made at pages 26-28, respondents' brief.

Had the point been raised below there would have been both occasion and opportunity to show the circumstances which made it necessary that the Bank so act and precisely what was done to inform the bondholders and to obtain the directions and supervision of the equity court in which the foreclosure proceedings were brought.

As this court has made this point one of the bases of

its opinion, we take the liberty of setting forth not only the law as it then existed, but also what was done by the trustee in order to show that there was nothing improper in the relationship of the trustee and the Committee.

In April of 1933 when the Committee was formed, Section 77B had not been enacted. If, therefore, a reorganization of the property was to be effected, it had to be done under then existing state laws, which meant that in some way and in some form title had to be acquired for the bondholders through state court foreclosure proceedings; for it was a fact *of which the courts took judicial notice* that properties such as the Granada could not then be sold for cash at anywhere near an adequate price at any sale and especially not at a forced sale under a foreclosure decree subject to the fifteen months' redemption period allowed by the laws of Illinois.

During the height of the depression in the real estate market, a number of courts of other jurisdictions, took cognizance of these facts and considering the situation to be emergent held that the Indenture Trustee had the right and was under the duty to bid in at the foreclosure sale for the benefit of all bondholders even though not authorized to do so by the terms of the Indenture and even over the objections of some of the bondholders that they were entitled to obtain their share of the proceeds in cash. See *Silver* v. *Wickfield Farms,* 227 N. W. 97 (Ia., 1929); *Hoffman* v. *First Bond and Mortgage Company of Hartford,* 164 Atl. 656 (Conn., 1933); *First National Bank of Wichita* v. *Neil,* 20 Pac. (2d) 528 (Kas., 1933).

In the latter case the court makes the additional point that the indenture trustee has the same rights as an individual mortgagee in the event of default and that one of the remedies is foreclosure, the trustee having the power to do whatever in its judgment is advisable to be done,—

not for the interest of one bondholder but for the best interests of all ratably, with authority, subject to the control of a court of equity, to adopt measures and to do acts which, though not specified in the trust indenture, are implied in its general directions and are reasonable and proper means for making them effectual.

In Illinois, however, it had always been the law that a trustee had no power to bid in for the bondholders in the absence of an express provision contained in the trust indenture.

Since the trustee could not bid and since there was no cash market, the only way in which the interests of the bondholders could be protected was through the formation of a committee which could acquire the property for the benefit of those who wished to participate and for those reasons the bank caused the Committee to be formed and financed it, for there was no financing available elsewhere. The holdings were small and widely scattered and there were no investors with interests large enough to justify their acting on a committee and with experience enough to contribute anything of value.

After the Committee was organized and on May 4, 1933, the bonds were called for deposit by letter (Appendix A hereto) in which, among other things, the bondholders were informed that the Bank was Indenture Trustee and that two of its officers were members of the Committee, and that the other members were officers of Cody Trust Company, one of the underwriters. The bondholders were told that the furniture litigation was pending in the Supreme Court of Illinois, and that it had been decided by the lower courts adversely to the Indenture Trustee.

Looking at it objectively, the only thing which the Bank could do if the interests of the bondholders were to be protected and enforced was to so form and support the Com-

mittee. See article by Mr. Justice Douglas in Harvard Law Review, February 1934, Vol. XLVII, No. 4, "Protective Committees in Railroad Reorganizations."

Nor, in forming the Committee, was it the Bank's purpose to perpetuate its own control or to protect itself from attack by the bondholders or to enhance its opportunities for profit. Any thought that there was intent to conceal the facts in relation to the furnishings is negatived by the letter, Appendix A. The record here shows that the Committee members were to get no compensation, that the Bank's charges for personnel and facilities furnished the Committee were at cost (R. 469), and that the great bulk of the properties which it was servicing were reorganized and that when they were the Bank surrendered possession as Trustee and has nothing to do with management, directly or indirectly. Moreover, in the Greenebaum issues, on some of the largest properties in Chicago, the Bank as Indenture Trustee, though requested, refused to enter into possession, although the management fees were much greater than those in this case. When 77B became operative the Bank cooperated in bringing many of its corporate reorganizations to the federal court. See respondents' brief, pages 56, 57, and R. 434.

Although, as we above pointed out, the law of Illinois had always been that an indenture trustee was without power to bid for the bondholders, in December of 1933 the Appellate Court of Illinois, in *Straus* v. *Chicago Title and Trust Company*, 273 Ill. App. 63, followed the decisions of the states above mentioned and held that in effect such proceedings, although nominally for foreclosure, were really actions for the enforcement of a trust of an active nature and that under circumstances requiring the exercise of such power the court might direct the trustee to act in a manner deemed for the best interests of the bondholders, including a trustee bid for all bondholders, notwithstanding that such action would not involve a cash sale.

Shortly afterwards, the Securities Act was amended to provide for exemption from registration of securities issued pursuant to a plan of reorganization approved by a court of competent jurisdiction, after notice to all persons to whom securities were to be issued of the hearing for approval at which they were entitled to appear and to be heard.

In this situation, the Indenture Trustee entertained genuine doubts as to what its powers were,—whether it should permit the property to be sold to the highest bidder for cash, whether it, itself, could and should bid in for all of the bondholders, or whether it would be better that the property be acquired pursuant to a Plan of Reorganization open to all bondholders to be submitted to and approved by the Court.

Accordingly, in July of 1934 it amended its cross-complaint for foreclosure (See Appendix B) and sought the directions and instructions of the court as to whether it should bid and if it should not, the approval of such Plan of Reorganization, if any, as might be adopted by the Committee and of the terms and conditions of the issuance or exchange of any securities under such plan, the plan to be carried out under the supervision and directions of the court. The Committee members were joined as defendants and a group of non-depositing bondholders were joined as representatives of the whole numerous class.

By October of 1935, the Illinois Supreme Court in *Chicago Title and Trust Company* v. *Robin,* 361 Ill. 261 reversed the Appellate Court and held that the Trustee was without power to bid in for the bondholders in the absence of authority contained in the Trust Indenture.

In view of this the decree of sale thereafter entered in the Granada foreclosure case did not direct the Trustee to bid, but did make the following provision:

"It is further ordered, adjudged and decreed that if

> it is the intention of said Committee acting under that certain Deposit Agreement dated April 26, 1933, relating to the bonds and interest coupons secured by said cross-complainant's said trust deed, or of any Committee now properly organized for the protection of the securities intended to be effected by said trust deed, to purchase the said real estate and premises involved herein and hereinabove described, pursuant to any plan or agreement of reorganization, that then prior to the time of sale the plan or agreement of reorganization be submitted to this court so that this court may determine whether or not the plan or agreement of reorganization is fair and reasonable and whether or not the terms and conditions of the issuance and exchange of securities pursuant to said plan or agreement of reorganization are fair and reasonable, and the court does hereby reserve jurisdiction to pass upon such matters and things and to provide for such notice as the court may deem proper to all persons to whom it is intended to issue securities in exchange or otherwise pursuant to such plan or agreement of reorganization." (Unprinted transcript, page 1059.)

Prior to the current 77B proceedings there was, of course, no plan adopted by the Committee and therefore no occasion to invoke the jurisdiction of the state court as above reserved.

Since the Committee as early as May, 1933 had already informed the bondholders that some of its members were officers of the Indenture Trustee and that others were officers of Cody Trust Company and since under the provisions of the Securities & Exchange Act and the Regulations relating thereto it was required that any plan disclose the affiliations of the Committee members, their interest, if any, in the securities of the Granada, and other relevant data, and since from the plain language of the amendment (Appendix B hereto) and of the above quoted portion of the decree, court approval of any plan was to be procured, it is not to be supposed that all of the facts would not have been disclosed to the court had a plan been

adopted, including the relationship of the Committee members to the Trustee and to one of the underwriters and the fact that Cody Trust Company owned 1000 shares of the common stock when it went into receivership in December of 1933.

Any sale under the decree was of course subject to the confirmation of the court without necessity for reservation of jurisdiction. Had the point been in issue, we would have shown that under existing state court practice the courts required an independent appraisal by the Chicago Real Estate Board in relation to any motion for the confirmation of a sale in bond issue foreclosures although it was true, as we have said, that there was no cash market in which anyone but the Committee would bid anywhere near the value. The Supreme Court of Illinois in *First National Bank* v. *Bryn Mawr Beach Bldg. Corp.*, 365 Ill. 409, 425, had laid down a formula for determining values to be accepted in such matters. The purpose of the appraisal was to satisfy the court that the amount of the bid plus the unpaid general property taxes, if any, was up to the fair economic value of the property. And we respectfully submit that the Committee "dominated" by the Bank, which was interested in all the investors, was more likely to make a fair bid than a committee completely independent of the Bank and interested in getting the property at the very lowest price.

We submit, therefore, that even if it be the rule that a bank ordinarily may not act as indenture trustee and at the same time sponsor a plan promulgated by a committee which it formed, nevertheless that action could be properly taken if, as in this case, the circumstances required it, and disclosure was made to the bondholders and to the court and court approval was obtained. On principle, the situation is no different than that referred to in Section 170.7 of Scott on Trusts relating to the purchase by a trustee

of trust property at its own sale,—generally improper, but permissible if done with the approval of the Chancery Court.

Scott says:

> "The reason why the permission or approval of the court is sufficient to justify a sale of trust property to the trustee personally is that a court of equity is a court having general supervision over the administration of trusts, and if the parties are properly represented before it, it has authority to authorize what would otherwise not be permissible."

We thus see that neither actually nor potentially was there any wrong in the fact that the trustee formed and dominated the Committee so far as any state court proceedings were concerned. And we submit that the application made by this court of the general principles concerning conflicts of representation appears all the more harsh when it is considered that this point was not raised below and that respondents therefore had no occasion to bring forward the facts herein mentioned which must necessarily be taken into consideration in exercising an equitable and conscionable discretion.

As to the Point That One of the Underwriters Represented on the Committee Not Only Owned the Common Stock of the Debtor Company But Was Later Claimed to Be Liable for Alleged Circular Misrepresentations.

As footnote 5, page 2 of the opinion, shows, Cody Trust Company went into receivership in December, 1933. The record shows that at that time it held 1,000 shares of the common stock of the debtor company. The record does not show when it acquired the common stock. But if there was any conflict of interest on the part of its officers who were members of the Committee, because of stock ownership, that conflict ceased to exist in December of 1933; for title to the stock then passed to the Receiver of Cody

Trust Company who later sold it to persons in no way connected with any of the Committee members (R. 220).

We have shown that by the terms of the decree of sale any plan of reorganization under which the Committee was to acquire the property in the foreclosure proceedings had to be submitted to the state court not only for approval of the plan but for approval of the terms and conditions of the issuance of the securities to be issued thereunder. We have shown that the requirements of the Securities and Exchange Commission were such that full disclosure of the ownership by Committee members, counsel and others connected with the plan, of any of the securities within five (5) years preceding the submission of the plan would have had to have been made in the plan itself. It follows that both the bondholders and the court would have been fully informed on this point under the procedure adopted by the Bank and to which it was irrevocably committed as shown by the above quoted portion of the decree.

If Cody Trust Company in May of 1933 owned any shares of common stock of the debtor company, it is true that the call letter, Appendix A hereto, made no mention of the fact. The letter was signed by the full Committee. If the fact is that at the time of the call letter the Cody Trust Company owned the common stock, then the failure to make disclosure thereof in the call letter might be grounds for disallowance of fees to the Committee members. But the Committee in this case did not request fees and certainly the knowledge of the Cody members of the Committee of the ownership in 1933 of the common stock by Cody, if it was then so owned, cannot be imputed to the City National Bank and Trust Company so as to deprive it of reimbursement for the expenses incurred in servicing the Committee.

As to the alleged circular misrepresentations, we showed

in our brief, pages 39, 48, that the Bank and counsel were without knowledge. As to counsel, this court accepts the statement. Neither this court nor the trial court made any finding that the Bank had knowledge and none would be justified on the record. We showed, at page 57, that even had there been knowledge, neither the Trustee nor the Committee had the right or power to take action, but that any cause of action was personal to those bondholders who were misled. The letter, Appendix A, informed the bondholders of the pending claim of the chattel mortgagee, of the litigation in relation thereto, its unfavorable termination in the lower courts, and of its pendency in the Supreme Court of Illinois.

Under these circumstances we submit that neither the ownership of the common stock for a short time by Cody nor the alleged circular misrepresentation is ground for total denial of compensation and reimbursement to the City National Bank and certainly not ground for denial of fees to counsel.

As to the Point That the Bank Was Also Indenture Trustee for Adjoining Properties and Dominated the Committees Representing Them, Although the Property of the Debtor Company Was Selling Service to the Other Two.

We show at pages 30-37 of our brief that the dealings between these properties did not constitute a breach of trust on the part of City National Bank and Trust Company. It had no interest individually in either property and held none of the securities. Its commissions for managing each property were in no way dependent upon the amount charged for the service furnished by the Granada. Nor did it ask for or receive any compensation for the work which it did in ascertaining the price to be fair. By the authorities cited, we have demonstrated that the situa-

tion was quite unlike that which exists when an agent acts for both buyer and seller in a transaction in which his compensation is dependent upon the consummation of the deal. The sole effect in this case was to put the burden upon the Trustee of showing that the price charged was fair and reasonable. The Court of Appeals found that it was, on the record, and this court accepted that finding in stating at page 2 of its opinion: "We agree with it that on this record recovery on the counterclaim would not be warranted"; for if the bank as trustee of the Granada had not charged enough its account would have been subject to surcharge and the counterclaim to that extent would have had to have been sustained. See Scott on Trusts, Section 170.16.

The cases cited by the court at page 5 of its opinion: *Jackson* v. *Smith*, 254 U. S. 586, 589, and *Weil* v. *Neary*, 278 U. S. 160, 173, are not in point. In the former case the court receiver, acting through two lawyers who were aware of his fiduciary position, without the knowledge of the court, acquired an interest in part of the property under the administration of the court, which interest was immediately resold at a substantial profit—a case of out and out fraud. In the other case, as the court states, there was involved a contract to split fees, which was in direct violation of the Rules in bankruptcy and which no doubt was surreptitiously entered into—again a case involving fraud or moral turpitude.

Even if the situation at bar involved a breach of trust, there was no fraud or moral turpitude involved, and the breach at most was merely technical. Not only that, but the transaction involved but a minute part of the entire administration of two complicated trusts, and therefore should not warrant the total disallowance of fees and reimbursement to the Trustee. Particularly is this true when the trial court's sole opinion reference to the Arlington property was "The burden is on it [City National] to

show that the changes which it made in amounts being charged for that service were warranted. I do not think it has met that burden." (R. 767)—a finding overruled by the Circuit Court of Appeals and said by this court to be without support in the record. In other words, the lower court never made the mere technical breach here involved a basis for the total disallowance of fees.

Only in case of a unitary plan (impossible for reasons shown at pages 16, 17, our brief), could there have been general conflict of interest in representation and in that event the limited conflict in reference to the interhotel services would have disappeared.

As to the Point That Counsel Represented Both the Indenture Trustee and the Committee in the Case of the Granada—

For the same reasons that it was proper for the Bank to act as Indenture Trustee and at the same time to form and to finance the Committee, it was proper for respondent-counsel to act both for the Trustee and the Committee. It is obvious that the primary purpose of all action taken in the state court and intended to be taken there was to acquire the property for the benefit of all bondholders by the only means available at a time when there was no market for cash, with full disclosure to the equity court and under its supervision and control both as to the fairness of any plan and as to the fairness of the price bid. What possible reason could there have been for incurring the expense of separate representation under the procedure which was followed in the state court proceeding?

As to the Point That Counsel Represented the Indenture Trustee and the Committees for the Adjacent Properties—

We have shown that there was no impropriety in the Bank's action in relation to those three properties, and for the same reasons it was proper for the respondent-attorneys to represent the Trustee and the Committees on all three. We have shown also that a conflict could have arisen only had there been a unitary plan of reorganization and that a unitary plan was never possible. See respondents' brief pages 16, 17, 31. That being so, there was no conflict between the several Committees and none in the services which counsel were to render to the Committees and to the Trustee in each foreclosure proceeding on these three separate issues.

As to the Point That Respondent-Attorneys Had Acted as General Counsel for Chicago Trust Company, "One of the Underwriters Whose Prospectus Was Under Attack in These Proceedings,"—

It is true that at the time the Granada bond issue was underwritten respondent-attorneys were general counsel for Chicago Trust Company and that they continued as general counsel for that bank until it was absorbed by The National Bank of the Republic in July of 1929. Respondent-attorneys, however, were never general counsel for The National Bank of the Republic nor for Central Republic Trust Company, which resulted from the consolidation of The National Bank of the Republic and Central Trust Company of Illinois, nor general counsel for City National Bank and Trust Company of Chicago. It is also a fact that the general counsel for Chicago Trust Company did not have to do with all legal matters and proceedings in which the Bank was interested. It had numerous attorneys and it had house counsel. And as respondent-attorneys

have represented and as the court has agreed, respondent-attorneys had nothing to do with the Granada circular.

The court states at page 4 of its opinion "and respondent-counsel had acted as general counsel for one of the two principal underwriters during the financing of the property here involved; and that underwriters' prospectus was under attack in these proceedings."

As we understand it, what the court means is that the Committee or the then Trustee, who were represented by respondent-attorneys, had some action against Chicago Trust Company for whom they had been general counsel, and that therefore there was a clash of interests in their representing the Trustee or the Committee. But, as we have pointed out, Chicago Trust Company had gone out of existence in 1931. Respondent-attorneys were no longer their general counsel and owed them no allegiance. How then, can it be said that the fact that respondent-attorneys had been formerly general counsel for Chicago Trust Company in any way disqualified them from acting as attorneys for the Committee or the Indenture Trustee in the 77B proceedings? Not only so, but, as we have shown, any cause of action on account of the circular misrepresentation was personal to the bondholders. Furthermore, if it was not personal to the bondholders, the cause of action in the 77B proceedings on behalf of the bondholders was vested in the Court Trustee and not in the Committee or Indenture Trustee.

As to Denial of Compensation for Services in the 77B Proceeding.

We submit that while the general principles laid down by the court in its opinion in reference to conflicts of interest are sound, and that while the court may have had some basis on the record alone for concluding that some of those principles were applicable in the instant case,

nevertheless in view of the facts as disclosed in this petition and the appendices hereto those principles are not applicable.

But even if the court, in view of the additional facts adduced, still be of the opinion that there was sufficient conflict of interest, and of important enough character, in the state court proceeding to be the basis for denial of any fees due on account of services there rendered, we submit that there is absolutely no ground for the denial of reimbursement to the bank for use by the Committee of its facilities and personnel and of reasonable compensation to counsel for their services in the 77B proceeding.

The only right which the Indenture Trustee had in the 77B proceeding was to file a claim on behalf of all the bondholders. The Committee had the sole function of formulating, presenting, and obtaining approval of a plan. The conflict, if any, which existed between the Indenture Trustee and the Committee in their functions in the state court proceeding ceased to exist. Likewise, as the only function of the Trustee was to file a claim on behalf of all bondholders, if there had been any conflict of interest in the representation by respondent-attorneys of both the Trustee and the Committee in the state court, that conflict of interest had also ceased.

Likewise, in the bankruptcy court, any conflict that had existed prior to the bankruptcy proceeding as to the sale of inter-hotel services had ceased to exist, for the Court Trustee was the representative of the Granada in those matters.

The record shows that the Committee was more than diligent in performance of its duties and formulated a plan and obtained its confirmation in record time, as well as the assents of its depositing bondholders and other creditors. The record further shows

that after the claims of the Court Trustee against the Committee, the Indenture Trustee, and their counsel had been filed and were under consideration by the court, the Committee was directed by the court to take the steps necessary to carry out the plan as confirmed. What basis then, in view of these facts and circumstances, can there be for denying to the Committee and to the attorneys all compensation on account of the services which they performed in the bankruptcy proceeding?

It is suggested by the court that the incidence of a particular conflict of interest can seldom be measured with any degree of certainty and that the bankruptcy court need not speculate as to whether the result of the conflict was to delay action where speed was essential, to close the record of past transactions where publicity and investigation were needed. But none of these observations are applicable to a determination of the right of the Committee and counsel to compensation for services in the bankruptcy proceeding, for clearly the incidence of any prior existing conflict of interest was not carried over into that proceeding. And certainly any conflict of interest which had existed prior to the institution of the bankruptcy proceedings and which had thereafter ceased to exist could not and did not have the effect to delay action in the bankruptcy court.

We quite agree that had there been a representation of conflicting interests in the bankruptcy proceedings the trial court would have been justified in denying compensation to respondents for the services there rendered. As the matter stands the rule as to denial of compensation is applied in a punitive way. Both in Scott on Trusts, Section 243, and in the American Law Institute Restatement, Trusts, Section 243, the basis for refusal of compensation to a trustee is not in the theory of a penalty but in the theory that payment is not due for services not

properly performed. That theory has been followed in the following cases:

Lydia E. Pinkham Medicine Company v. *Gove*, 20 N. E. (2d) 482, 486 (Mass.).

In re Card's Estate, 9 Atl. (2d) 557, 560 (Pa.).

In re Keen's Estate, 159 Atl. 713, 715 (Pa.).

In re Johnston's Estate, 14 Atl. (2d) 469, 473 (N. J.).

Pierce v. *Dahlgren*, 300 Fed. 268, 272 (C. C. A. 6).

Purdy v. *Johnson*, 248 Pac. 764, 770 (Cal.).

In the case of *Lydia E. Pinkham Medicine Company* v. *Gove*, 20 N. E. (2) 482, at page 486, the court recognizes the rule to be that a trustee who commits a breach of trust or an agent guilty of disloyal conduct thereby imperils his right to compensation, but adds "but the rule is not an inflexible one. Each case must be determined in the discretion of the court with reference to the peculiar factors found to be present. Although pure considerations of public policy have no doubt weighed heavily against fiduciaries who have placed selfish interest above duty, yet the American Law Institute finds the basis for refusal of compensation to a trustee not in the theory of a penalty but in the theory that payment is not due for service not properly performed * * *. Apparently upon similar reasoning a disloyal agent may have compensation which is 'apportioned' by the contract of employment to services properly performed."

Of course, if a breach of trust involves moral turpitude, the foregoing rule would not be applicable and it would be just and equitable that the respondents be denied compensation even for such services as were properly performed. But in this case there was no moral turpitude because the breach of fiduciary duty, if any, was not motivated by self-seeking or self-gain, but was the result of the exigencies of the situation which called for action

of some kind to obtain for the *cestui que trustents* effective results.

Conclusion.

We submit that in view of all the facts and circumstances there were not even technical breaches of trust in this case. But even if there were, no moral turpitude was involved, and to deny all compensation because of technical breaches of trust which affected only a small portion of the services performed is to put denial of compensation on a punitive basis, when the law heretofore has always been that denial of compensation in such cases should be on a compensatory basis.

We therefore submit that if technical breaches were shown it should not have resulted even in denial of all compensation for all of the services performed in the state court proceeding and certainly should not have affected the compensation for services performed in the 77B proceeding. For to do away with all pre-existing distinctions in the results of mere technical breaches and breaches involving moral turpitude is to put them on the same level of conduct.

Respectfully submitted,

VINCENT O'BRIEN,
JOHN MERRILL BAKER,
TRACY WILSON BUCKINGHAM,
Attorneys for Respondents.

CERTIFICATE OF COUNSEL.

I, Vincent O'Brien, one of the attorneys for the respondents, do hereby certify that the above and foregoing petition for rehearing is presented in good faith and not for delay.

....

APPENDIX A.

Bondholders' Protective Committee
208 South La Salle Street
Chicago, Illinois

Howard E. Green, Secretary
Franklin 7400

Marley Halvorsen, Ass't Secretary
Randolph 6600

Committee	Depositary
Charles S. Tuttle	Central Republic Trust Company
Edward S. Clark	Room 440, 208 South La Salle Street
Lewis W. Riddle	Chicago, Illinois
W. G. Sturm	

May 4, 1933.

To the Holders of

The Granada

(Unsubordinated) First Mortgage Six Per Cent Real Estate Gold Bonds, dated September 1, 1928
Executed by Granada Hotel Corporation

These bonds were originally issued in the principal amount of $525,000, of which certain bonds of the final maturity totalling $25,000 were expressly subordinated at the outset to the remaining bonds as to the lien of the trust deed given to secure the issue. $486,500 of the unsubordinated bonds and all of the subordinated bonds are now outstanding. This letter is directed to the holders of the unsubordinated bonds only.

Default has been made in the payment of the March 1, 1932, September 1, 1932, and March 1, 1933, interest coupons pertaining to unsubordinated bonds in the total amount of approximately $43,100, and also in the payment

of the principal of unsubordinated bonds which matured on the same dates amounting to $24,000.

The unsubordinated bonds were underwritten jointly by Chicago Trust Company (since succeeded by Central Republic Trust Company) and Cody Trust Company, $300,000 of bonds being offered by Cody Trust Company and $200,000 by Chicago Trust Company. Central Republic Trust Company is Successor Trustee under the Trust Deed executed by Granada Hotel Corporation to secure these bonds.

The property covered by this Trust Deed, commonly known as The Granada, located at 525 Arlington Place, Chicago, Illinois, is a five story and basement fireproof apartment hotel, containing 114 suites of one, two, three and four rooms, each with bath.

In the summer of 1930 action was commenced to partially foreclose a second mortgage on this property. A receiver was appointed in that proceeding under an order providing for the continuation of the existing management and the payment to the receiver of the net income from the property after the payment of operating expenses. Statements furnished by the receiver show that the net income thus paid to the receiver has, except for a small current balance, been paid over by it to Central Republic Trust Company, as Trustee, under orders of court directing its application on interest and principal installments maturing on these bonds on September 1, 1931, and prior thereto, and also in reimbursement of the Trustee for certain advances made by it in respect of these bonds.

The net income applied in this manner to meet the interest and principal requirements of these bonds has, how-

ever, been inadequate for that purpose. Annual interest at 6% on the outstanding unsubordinated bonds amounts to $29,190, and fixed prepayments are now $17,500, a total of $46,690.

As an incident to this foreclosure action the right of the holder of a chattel mortgage covering some of the furnishings and equipment in the building to remove such property pursuant to a foreclosure sale under the chattel mortgage has been contested by the Trustee under the Trust Deed securing these bonds on the ground that the property in question is part of the real estate covered by that Trust Deed. This contest has been decided by the lower courts adversely to the Trustee, and a review by the Supreme Court of Illinois is now being sought.

In addition to the defaults in the payment of interest and principal maturities, unpaid taxes on this property have accumulated over several years. Total general property tax liabilities, exclusive of interest and penalties, have been reported as follows:

1928 (property sold for non-payment)	$ 8,692.30
1929 (protested)	10,222.40
1930 (protested)	11,199.06
1931 (recently billed, protested)	10,431.38
Total	$40,545.14

Taxes for 1932 and 1933, although not yet payable, constitute liens against the property which, together with liens for past due taxes, take priority over the lien of the trust deed securing these bonds. Cody Trust Company purchased and now holds the certificate of sale for 1928 taxes.

In view of these defaults, accumulated tax liabilities and the apparent inadequacy of the net income from the property, it has been deemed necessary to form a Committee for the protection of the holders of the unsubordinated

bonds, and to call for the deposit of these bonds with Central Republic Trust Company, 208 South La Salle Street, Chicago, Illinois, Depositary for the Committee.

The Committee has been constituted under a Deposit Agreement dated April 25, 1933. Holders of unsubordinated bonds who deposit their bonds become parties to that Agreement. Copies of the Agreement are on file with the Depositary and with Cody Trust Company, 105 South La Salle Street, Chicago, Illinois, where they may be examined by any holder of these bonds.

It is anticipated that action to foreclose the Trust Deed securing these bonds may be instituted by the Trustee in the near future and this Committee will probably find it advisable to develop some plan for the reorganization of the financial structure of this property.

Mr. Tuttle and Mr. Sturm are Vice Presidents of Central Republic Trust Company and Mr. Riddle and Mr. Clark are President and Assistant Secretary, respectively, of Cody Trust Company. The Deposit Agreement provides that the members of the Committee shall receive no compensation for their services.

The speed with which plans for protecting the interests of holders of these unsubordinated bonds can be formulated will depend largely upon the promptness with which the bonds are deposited. We feel that it is important for the protection of your interests that you send your bonds to the Depositary promptly.

For your convenience, we enclose herewith a blank form of Letter of Transmittal to be used in this connection. Full instructions as to how to fill out this Letter are given on the reverse side.

As soon as possible after receipt of your bonds (accompanied by such Letter of Transmittal) the depositary will

mail to you a transferable certificate covering the bonds you have deposited.

C. S. Tuttle,
Chairman,
Edward S. Clark,
Lewis W. Riddle,
W. G. Sturm.

Holders of bonds payable at
Chicago Trust Company
address all communications to:
Howard E. Green,
Secretary,
208 South La Salle St.,
Chicago.

Holders of bonds payable at
Cody Trust Company
address all communications to:
Marley Halvorsen,
Ass't Secretary,
105 South La Salle St.,
Chicago.

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APPENDIX B.

STATE OF ILLINOIS, }
COUNTY OF COOK. } ss.

IN THE SUPERIOR COURT OF COOK COUNTY.

In Chancery.

William A. Thuma, *Complainant*, *vs.* Granada Hotel Corporation, *et al.*, *Defendants.*	Bill. No. 519151. Cross-Bill.
Central Republic Trust Company, etc., *Cross-Complainant*, *vs.* Granada Hotel Corporation, *et al.*, *Cross-Defendants.*	

AMENDMENT TO CROSS-BILL OF COMPLAINT AS HERETOFORE SUPPLEMENTED.

Now comes Central Republic Trust Company, a corporation, as Trustee under Trust Deed recorded in the Recorder's office of Cook County, Illinois, as Document 10161996, and as Chattel Mortgagee under Chattel Mortgage recorded in the Recorder's Office of Cook County, Illinois, as Document B702627, and leave of Court being first had and obtained, files herein this, its Amendment to the Cross-Bill of Complaint as heretofore supplemented as follows:

1. Immediately following Paragraph 7 of the original cross-bill of complaint, insert the following:

"(a) That upon the happening of the defaults hereinabove mentioned the trust evidenced by your orator's said indenture became active. Your orator is advised by counsel, and therefore states the fact to

be, that thereupon it became its primary duty under the terms of said indenture, on proper demand and indemnity, to conserve the trust property for the benefit of the beneficiaries, to-wit: The holders of the bonds and coupons secured by its said indenture, and to administer and distribute the trust estate or the proceeds or avails thereof to the best interests of its said beneficiaries, and on demand by said beneficiaries, accompanied by indemnity satisfactory to your orator, as required in said indenture, to take any action to conserve, protect and enforce all rights under said indenture; and it became its right, at its option, without such demand and indemnity, to take such action if it should see fit so to do. Your orator further avers that one of the methods available to enable it to carry out its primary duty aforesaid is that of foreclosure and sale of the property covered by said indenture to the highest and best bidder for cash, but it is informed and believes and therefore represents the fact to be that proceedings seeking merely the foreclosure of similar indentures securing similar bond issues and sale at public auction to the highest and best bidders for cash have usually failed to result in adequate outside cash bids, and that such failure is particularly prevalent now because of the current depression which has continued for a long time past and still continues not alone throughout the County of Cook but throughout the United States, of which depression your orator prays that the court take judicial notice. Because of the prevailing conditions incident to said depression it has been and still is very difficult to borrow money with which to pay the costs and expenses of foreclosure proceedings, and, in cases in which some of the holders of bonds secured by a trust deed which has been foreclosed have wished to combine directly or indirectly to purchase at foreclosure sale premises covered by such trust deed for the protection of their interests, it has been difficult to provide funds to pay in cash the distributive share of the purchase price of bondholders not wishing to join in such purchase, except in cases in which substantially all of the bondholders have combined to acquire the property at such sale. Under these conditions it is hazardous for a trustee under a trust deed to proceed to a decree of foreclosure which may be executed only by sale of the mortgaged property

to the highest and best bidder for cash, save only in those cases in which the bondholders have not only combined to protect their interests through purchase at the foreclosure sale but have adequate cash to enable them to pay such costs and expenses and to provide for bondholders who do not wish to join in such purchase their distributive share of a bid which is sufficient in amount adequately to protect the interests of the bidders.

"Your orator further represents that it is advised by counsel that the method of sale for cash is but one of the methods available to it in and about the protection, preservation and enforcement of the rights and interests of its said beneficiaries, and that, due not only to difficulties inherent in trusts of this type but also to those arising because of the current depression, other means and methods may be required for the best protection, enforcement, and administration of said trust. Your orator avers that the protection, enforcement, and administration of the said trust and the distribution of the trust estate involve questions concerning the construction and effect of the trust powers conferred upon your orator in and by its said trust indenture or implied by law as necessary to the preservation, enforcement, administration, and distribution of the trust and of the trust property, which questions must be determined and adjudged by this court. Some of such questions are whether your orator is vested with power to bid at any foreclosure sale for and on behalf of all of its beneficiaries and, if so, whether the facts, circumstances, and conditions obtaining in this case require the exercise of such power; whether your orator should permit the property to be sold under existing conditions at public auction to the highest and best bidder for cash or whether the court should specify a price below which the property may not be sold; or whether it is to the best interests of the beneficiaries that a plan or agreement of reorganization or readjustment be formulated, presented, developed, approved, promulgated and adopted, and, if so, whether in such plan participation should, at the instance of the participating beneficiaries, be granted or allowed to persons having claims or any interests junior or senior to those secured by your orator's said indenture, or to any persons having an interest in the trust property or

property used in connection therewith. Moreover, your orator avers that it is advised by counsel and therefore states the fact to be that there is a question as to whether the powers of your orator under the trust indenture in this case should be enlarged, modified or changed because of existing conditions and the circumstances in this case in order to prevent loss to the beneficiaries, and that such question should be presented to and be passed upon by this court. From time to time during the pendency of this proceeding other questions may arise and be presented to this court, the determination of which will require an interpretation of the provisions of the trust indenture.

"Your orator further avers that it is in doubt as to the nature and extent of its powers and duties in the premises and that, in view of the inherent difficulties and of the prevailing conditions confronting it in respect of the protection, enforcement and administration of its said trust, some of which conditions may not have been within the contemplation of the parties to the trust at the time of the creation thereof, and because of its doubts as to the nature and extent of its powers and duties in the premises, it is essential that the provisions of the trust indenture be construed and that the nature and extent of its powers and duties be defined in relation to the existing facts and circumstances.

"By reason of the premises your orator avers that it is essential that it receive the advice, instruction, and direction of this court as to the nature and extent of its powers and duties and as to the exercise of its powers and the course of action to be pursued by it in proceeding to protect and to enforce the trust intended to be effected by its said indenture, which advice, instruction and direction in the premises your orator hereby requests."

"(b). That while your orator, under and by virtue of the terms and provisions of its said trust indenture, is authorized and empowered to act as the representative of the bondholders in and about any proceeding for the foreclosure of the mortgage evidenced thereby, yet, in so far as your orator seeks the construction and definition of the trust evidenced by the said indenture and the advice, instruction, and direction of this court in

respect of the protection and enforcement of the trust, the said beneficiaries, to wit: the holders of the unpaid bonds and interest coupons described in and secured by the said indenture, are necessary and indispensable parties to this proceeding."

"(c). That certain of the bonds secured by your orator's said indenture, with certain unpaid interest coupons pertaining thereto, have been deposited with and are held and owned by C. S. Tuttle, Edward S. Clark, Lewis W. Riddle, W. G. Sturm, and E. A. Kilmer, not individually but as a Committee acting under the certain deposit agreement dated April 26, 1933, relating to the bonds of the issue secured by your orator's said indenture, and that such bonds and the unpaid interest coupons thereunto pertaining are so held and owned by said Committee subject to all the terms and provisions of the said agreement last aforesaid, and that your orator therefore makes the said C. S. Tuttle, Edward S. Clark, Lewis W. Riddle, W. G. Sturm, and E. A. Kilmer, not individually, but as members of the aforesaid Committee, parties defendant to this, its Cross-bill of complaint."

"(d). That the remaining unpaid bonds described in and secured by your orator's said indenture, and unpaid interest coupons pertaining thereto, have not been deposited with, and are not now owned and held by, the Committee aforesaid, but are held and owned by more than one hundred persons; that all and each of said bonds and the unpaid interest coupons thereunto pertaining are payable to bearer, and that accordingly title thereto passes by mere delivery, and that it is impracticable, if not impossible, to determine as of any given date the names and addresses of all of the holders and owners of such bonds and of the unpaid interest coupons aforesaid thereunto pertaining. Your orator further avers that the holders and owners of the bonds and coupons last aforesaid reside in different cities and communities throughout the United States, many without the State of Illinois; that the expense and delay incident to making the holders thereof parties defendant hereto by name and in person would be prohibitive and would tend to impair the administration of justice. But your orator avers that the interests of each and every the holders and owners of the said bonds and coupons not deposited with the said Committee are

common and identical, and that the interest of no one of the holders of such bonds and coupons is in conflict with the interest of the holders of the other bonds and coupons not so deposited; that your orator has selected from the holders and owners of the said nondeposited bonds whose names and addresses are known to your orator a sufficient number thereof, to wit: fourteen (14), who hold and own nondeposited bonds aggregating $11,800.00 in principal amount, truly to represent the interests of the holders and owners of all nondeposited bonds as a class, and hereby makes such persons so selected, to-wit: A. W. Childs, M. M. Kraft, Amanda Jahnke, Grace Tripoli, Hugh Hamill, Eli Goldstein, Mrs. S. E. Lebovitz, W. P. Naumes, Catherine Cline, George H. Tallaksen, Rose Golden, Artie Cowper, Emil Ismaiel, and Esther Settem, parties defendant to this, its Cross-bill of complaint, as representative of all of the holders and owners of said nondeposited bonds as a class, subject, however, to the right of any such bondholder not made party defendant hereto by name to be and become a party defendant hereto by name and to defend this suit in his own behalf."

2. After the name Margaret Schuster appearing in the prayer of the original Cross-bill of complaint, insert the following: C. S. Tuttle, Edward S. Clark, Lewis W. Riddle, W. G. Sturm, and E. A. Kilmer, not individually, but as a Committee acting under Deposit Agreement dated April 26, 1933, relating to bonds of the Granada Apartments issue; A. W. Childs; M. M. Kraft; Amanda Jahnke; Grace Tripoli; Hugh Hamill; Eli Goldstein; Mrs. S. E. Lebovitz; W. P. Naumes; Catherine Cline; George H. Tallaksen; Rose Golden; Artie Cowper; Emil Ismaiel; and Esther Settem, individually and as representatives of all other holders of Granada Apartments bonds similarly situated.

3. Immediately before the words "and that your orator may have such other and further relief as equity may require and to the court may seem meet," appearing on Page 16 at the conclusion of the prayer of the original

Cross-bill of complaint and preceding the prayer for process, insert the following:

"That the Court may determine and find that it has jurisdiction of each and every the parties hereto, including all the holders of unpaid bonds or coupons secured by plaintiff's trust deed, whether such holders are made parties hereto by name or brought in by representation as aforesaid; that the court may find that it has jurisdiction of the subject matter hereof, including jurisdiction of any plan or agreement of reorganization or readjustment or for the protection, preservation, or distribution of the trust property, including any amendment to such plan or agreement; that the Court may find that it has jurisdiction to determine the fairness of the terms and conditions of the issuance or exchange of any securities to be issued pursuant to such plan or agreement or amendment thereof, and of any certificates of deposit issued by the said Committee or its depositary to holders of bonds or interest coupons issued under said indenture, or any of them, and that the Court may find that it has jurisdiction to approve the said plan of agreement or amendment thereof, and to approve the terms and conditions of the issuance or exchange of any such securities or certificates of deposit.

"That the Court may determine the nature and extent of the powers and duties devolving upon the plaintiff in the premises by reason and by virtue of its trust indenture aforesaid and the conditions and circumstances obtaining in respect of the trust property, and that to that end the Court may determine and define the provisions of the trust indenture creating such powers and may determine and define those powers, if any, existing by implication of law on account of the facts and circumstances now existing, and that in that regard the court may also determine the existence of the emergency hereinabove referred to and its effect, if any, upon the trust, its administration and liquidation, and that it may generally hear and determine all questions which may exist or which may be raised in relation to the said trust, its administration, or liquidation, and may instruct and direct the plaintiff as to its powers, duties, and obligations in the premises.

"That the Court may inquire into all the facts and circumstances relating to the preservation and enforce-

ment of the trust and the distribution of the trust property, and then determine whether a sale of the mortgaged property should be decreed to the highest and best bidder for cash, or whether the court should specify in its decree a price below which the property may not be sold, and authorize and direct your orator to bid at any foreclosure sale for the benefit of its beneficiaries an amount equal to the price so specified unless someone else bids that amount or more, if it be found that your orator has the power so to bid and that the existing facts and circumstances call for the exercise of such power; that the Court prescribe in its decree the means and method to be employed in the administration, liquidation or distribution of the trust property in the event that the plaintiff does so bid; that the Court further determine whether it is for the best interests of the said beneficiaries that a plan or agreement of reorganization, readjustment, or liquidation be formulated, presented, developed, approved, promulgated, or adopted as the best means to protect and enforce the rights and interests of the said beneficiaries, and in such case that the Court may examine and inquire into any such plan or agreement, determine whether participation in such plan or agreement may at the instance of the participating beneficiaries be given to interests and claims other than those secured by the plaintiff's said trust indenture; that the Court may determine whether such plan or agreement, or the terms and conditions of the issuance or exchange of any securities to be issued pursuant to such plan or agreement, or of any certificates of deposit issued by said Committee or its depositary to holders of bonds or interest coupons issued under said indenture are fair and equitable, and if so, that it may approve such plan or agreement and the terms and conditions of the issuance or exchange of any such securities or certificates of deposit, and that if such approval be decreed the Court reserve a continuing jurisdiction to insure the carrying out of such plan in the event that the mortgaged property is purchased in pursuance thereof at any sale that may be had herein.

"That in any accounting to be taken herein there be fixed and allowed to your orator as additional indebtedness secured by the lien of its said trust indenture prior to the lien thereof as security for the payment

of bonds and coupons thereby secured and in addition to the items hereinabove prayed to be allowed on the taking of such accounting, any and all sums advanced by your orator pursuant to the provisions of its said trust deed or to any decree or order of court herein for any purpose authorized or permitted by the terms and provisions of said trust deed, decree, or order, with interest thereon at the rate of seven per cent (7%) per annum from the time of such advance or disbursement until reimbursement therefor, and also for any and all special fees and expenses of your orator and of its counsel incurred in and about the protection, enforcement, administration, and liquidation of its said trust, and that any and all sums so fixed and allowed in any accounting be decreed to be secured by a valid and subsisting first lien upon the trust property, the proceeds, avails, and income thereof, prior to the lien of the holders of bonds and coupons secured by your orator's said trust deed, and that prior to the transfer or disposition of such trust property adequate provision be made by the court for the protection and security of your orator's said lien."

Central Republic Trust Company, as Trustee,

By ....,
Its Solicitors.

....,
Solicitors for said Cross-Complainant.

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SUPREME COURT OF THE UNITED STATES.

Nos. 281 and 282.—October Term, 1940.

Weightstill Woods, Court Trustee, Petitioner, 281 *vs.* City National Bank and Trust Co. of Chicago, et al.	On Writs of Certiorari to the United States Circuit Court of Appeals for the Seventh Circuit.
Weightstill Woods, Court Trustee, Petitioner, 282 *vs.* City National Bank and Trust Co. of Chicago, et al.	

[February 3, 1941.]

Mr. Justice Douglas delivered the opinion of the Court.

The basic question involved in this case concerns the power of the District Court in proceedings under Ch. X of the Chandler Act[1] (52 Stat. 840) to disallow claims for compensation and reimbursement on the grounds that the claimants were serving dual or conflicting interests. The claimants, respondents here, are an indenture trustee, a bondholders' committee, and the committee's counsel. Counsel to the committee was also counsel to the indenture trustee; and its services in the latter capacity were included in the claim of the indenture trustee. The bankruptcy trustee appeared in opposition to the allowance of these claims, and counterclaimed against the indenture trustee seeking to surcharge it for various alleged acts of misconduct and negligence. The indenture trustee answered. There

1 This reorganization started with foreclosure proceedings in the Illinois state court and later was transferred to the United States District Court upon the filing of petitions under § 77B of the Bankruptcy Act. Pursuant to § 276(c)(2) of the Chandler Act, the bankruptcy court made that chapter applicable to the allowance of these claims. The claims under review cover not only the proceedings under § 77B but also the earlier state court proceedings. Though some of the allowances here in issue apparently had been fixed by the state court prior to the transfer of the proceedings to bankruptcy, respondents agreed to submit the claims *de novo* to the District Court.

was a hearing on the claims and on the counterclaim. The District Court disallowed the claims "for want of equity"; and allowed the counterclaim only as a recoupment to extinguish any claims of respondents. On appeal the Circuit Court of Appeals reversed. 111 F. (2d) 834. It held that there was no conspiracy to defraud, nor substantial evidence of mismanagement or negligence on the part of respondent-trustee. It thereupon remanded the cause to the District Court, indicating that the out-of-pocket expenses should be allowed in full and that the reasonable and customary charge for services so rendered should govern the claims for compensation. We granted the petition for writs of certiorari[2] in view of the importance in reorganization proceedings of the power of the District Court over such allowances.

We are not inclined to question the conclusion of the Circuit Court of Appeals on the issue of fraud. We agree with it that on this record recovery on the counterclaim would not be warranted. But we do not believe it was justified in disregarding the evidence and findings of fact as respects respondents' dual or conflicting interests in this reorganization.

The property here involved is an apartment hotel—Granada Apartments, Inc. A committee was formed by the respondent-trustee[3] to represent the first mortgage bonds in the reorganization. It was composed of five members. Two of these were officers or employees of one of the principal underwriters of the bonds.[4] This underwriter was heavily interested in the equity.[5] So far as appears, that fact was not disclosed when the committee solicited the bondholders. In any event, the equity owner is peculiarly ill-suited to represent the mortgagee in these situations because of their historic clash of interests. See *Case* v. *Los Angeles Lumber Products Co.*, 308 U. S. 106. Furthermore, a rather serious question was raised

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[2] The two cases raise the same question. One represents an appeal to the Circuit Court of Appeals as of right; the other an appeal with leave. They were taken prior to our decision in Dickinson Industrial Site *v.* Cowan, 309 U. S. 382. And see Reconstruction Finance Corp. *v.* Prudence Securities Advisory Group, No. 69, decided Jan. 6, 1941.

[3] Not then the trustee under the indenture.

[4] A third member was also a distributor of the bonds when they were publicly offered.

[5] This underwriter—Cody Trust Co.—went into receivership in December, 1933, the Granada bondholders' committee having been formed in April, 1933. The District Court found that nominees of Cody Trust Co. operated the property until January, 1934.

early in this reorganization concerning alleged misrepresentations by the underwriters on the sale of the bonds that the furnishings of the hotel were covered by the mortgage. It turned out that they were not; and bondholders' money was used to satisfy the lien outstanding against them.[6] Objective scrutiny and full enforcement of an underwriter's liability requires a committee freed from that underwriter's influence.

The committee was closely affiliated with the respondent-trustee, which, as we have noted, caused its formation. And respondent-trustee was in turn later appointed as successor trustee under the mortgage on petition of the committee. The committee had as its two most active members officers of the indenture trustee. It was in substance a part of the indenture trustee's reorganization division.[7] The indenture trustee was the committee's depositary; it would receive any fees accruing to the committee. Indenture trustees themselves have frequently condemned such entanglements with committees.[8] The indenture trustee represents all the bondholders; the committee those who have given it authorizations — in this case about 50 per cent. Where the interests of majorities and minorities do not coincide, the interests of the indenture trustee and the committee will tend to be antagonistic.[9] Beyond that is the fact

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The reorganization began with a foreclosure proceeding in the state court. The indenture trustee, predecessor of respondent trustee, later took possession and employed a so-called agent at $50 per month "to keep Cody Trust Company informed as to the status from time to time."

6 Certain phases of the litigation involving this question are revealed in Thuma *v.* Granada Hotel Corp., 269 Ill. App. 484; Wenstrand *v.* Pick & Co., 38 F. (2d) 25; In re Granada Apartments, Inc., 104 F. (2d) 528.

So far as appears no effort was made in this reorganization to assert any claim against the underwriters.

7 That division had handled over 400 reorganizations, having been formed to act in connection with defaulted bond issues underwritten by Chicago Trust Co. and Central Trust Co. of Illinois. Chicago Trust Co. was one of the underwriters of the Granada bonds.

8 Utter, Problems of Trustees Under Defaulted Bond Issues, 56 Trust Companies 653 (1933); Littleton, Administration Problems Under Corporate Trusteeship, *id.*, 335, 338.

9 Utter, *op. cit. supra* note 8, pp. 656-657. That antagonism was best illustrated in foreclosure reorganizations where the minority was not bound to accept new securities but could insist on cash. See Weiner, Conflicting Functions of the Upset Price in a Corporate Reorganization, 27 Col. L. Rev. 132. In the instant case the reorganization proceeding was in the state court from June, 1930 when a receiver under the second mortgage was appointed to May, 1937 when petitions under § 77B of the Bankruptcy Act were approved. For an earlier and unsuccessful attempt to place this company under § 77B see Tuttle *v.* Harris, 297 U. S. 225. Respondent-indenture trustee became such in January, 1935. It was in possession from then until May, 1937.

that an indenture trustee closely affiliated with a committee shares the committee's conflicts of interest.

In this case the indenture trustee was also indenture trustee for neighboring apartment properties and dominated the committees representing the bonds of those other companies. Two members of respondent committee were also members of one of those other committees. There was no unitary plan of reorganization for these several properties. But there were dealings between them by their common representatives—dealings attacked by petitioner as unfair to the instant company and defended by respondents as fair.

That is not all.

Counsel to the committee was not only counsel to the indenture trustee in this reorganization; it was also counsel to the indenture trustee and the committees for the neighboring properties. And respondent-counsel had acted as general counsel for one of the two principal underwriters[10] during the financing of the property here involved; and that underwriter's prospectus was under attack in these proceedings.[11]

Under Ch. X of the Chandler Act the bankruptcy court has plenary power to review all fees and expenses in connection with the reorganization from whatever source they may be payable.[12] Reasonable compensation for services rendered may be allowed.[13] The claimant, however, has the burden of proving their worth. Furthermore, "reasonable compensation for services rendered" necessarily implies loyal and disinterested service in the interest of those for whom the claimant purported to act. *American United Mutual Life Ins. Co.* v. *City of Avon Park,* No. 31, decided Nov. 25, 1940. Where a claimant, who represented members of the investing public, was

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[10] Chicago Trust Co., which was also the original indenture trustee.

[11] Respondent-counsel denies that it acted as counsel in that particular transaction or knew of the alleged misrepresentation in the prospectus at the time, and asserts that it did not learn of the contents of the circular until a question was raised concerning it during this reorganization proceeding. We accept its version of the facts.

[12] Sec. 221(4) provides: "The judge shall confirm a plan if satisfied that . . . all payments made or promised by the debtor or by a corporation issuing securities or acquiring property under the plan or by any other person, for services and for costs and expenses in, or in connection with, the proceeding or in connection with the plan and incident to the reorganization, have been fully disclosed to the judge and are reasonable or, if to be fixed after confirmation of the plan, will be subject to the approval of the judge; . . . ."

[13] Indenture trustees, committees, and their attorneys are included among those to whom the compensation may be allowed. § 242.

serving more than one master or was subject to conflicting interests, he should be denied compensation. It is no answer to say that fraud or unfairness were not shown to have resulted. Cf. *Jackson* v. *Smith*, 254 U. S. 586, 589. The principle enunciated by Chief Justice Taft in a case involving a contract to split fees in violation of the bankruptcy rules, is apposite here: "What is struck at in the refusal to enforce contracts of this kind is not only actual evil results but their tendency to evil in other cases." *Weil* v. *Neary*, 278 U. S. 160, 173. Furthermore, the incidence of a particular conflict of interest can seldom be measured with any degree of certainty. The bankruptcy court need not speculate as to whether the result of the conflict was to delay action where speed was essential, to close the record of past transactions where publicity and investigation were needed, to compromise claims by inattention where vigilant assertion was necessary, or otherwise to dilute the undivided loyalty owed to those whom the claimant purported to represent. Where an actual conflict of interest exists, no more need be shown in this type of case to support a denial of compensation.

Protective committees, as well as indenture trustees, are fiduciaries. *Bullard* v. *City of Cisco*, 290 U. S. 179; *Jewett* v. *Commonwealth Bond Corp.*, 241 App. Div. 131; *Bergelt* v. *Roberts*, 144 Misc. 832, aff'd 236 App. Div. 777; *Carter* v. *First Nat'l Bank*, 128 Md. 581. Cf. *Nichol* v. *Sensenbrenner*, 220 Wis. 165. A fiduciary who represents security holders in a reorganization may not perfect his claim to compensation by insisting that although he had conflicting interests, he served his several masters equally well or that his primary loyalty was not weakened by the pull of his secondary one. Only strict adherence to these equitable principles can keep the standard of conduct for fiduciaries "at a level higher than that trodden by the crowd." See Mr. Justice Cardozo in *Meinhard* v. *Salmon*, 249 N. Y. 458, 464.

The findings of the District Court that these claimants represented conflicting interests are amply supported by the evidence.

Some discrimination, however, is necessary in applying the foregoing rule to claims for expenses. Reimbursement for "proper costs and expenses incurred in connection with the administration" of the estate may be allowed.[14] The rule disallowing compensation because of conflicting interests may be equally effective to bar recovery of the expenditures made by a claimant subject to conflict-

[14] Sec. 242.

ing interests. Plainly expenditures are not "proper" within the meaning of the Act where the claimant cannot show that they were made in furtherance of a project exclusively devoted to the interests of those whom the claimant purported to represent. On the other hand, those expenditures normally should be allowed which have clearly benefitted the estate. Scott on Trusts (1939), § 245.1. Thus where taxes have been paid, needful repairs or additions to the property have been made, or the like, equity does not permit the estate to retain those benefits without paying for them. Such classification of expenses, at times difficult, rests in the sound discretion of the bankruptcy court. The District Court drew no such distinction but proceeded on the theory that reimbursement for all expenses must be denied. But it is not apparent that all of them fall within the prohibited category.

The other points raised by petitioner are so plainly without merit that they do not warrant mention.

For the reasons stated we reverse the judgment of the Circuit Court of Appeals and remand the cause to the District Court for further proceedings in conformity with this opinion.

It is so ordered.

A true copy.

Test:

Clerk, Supreme Court, U. S.